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PROVISIONAL INTELLIGENCE REPORT

MOBILIZATION AND ALLOCATION OF RESOURCES THROUGH THE NATIONAL BUDGET OF COMMUNIST CHINA 1950-55



CIA/RR PR-143

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THROUGH THE NATIONAL BUDGET OF COMMUNIST CHINA
1950-55

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(ORR Project 15.850)

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FOREWORD

This report attempts to identify and evaluate the source of the revenue which is subject to control and allocation through the national budget of Communist China; to estimate the proportionate contributions of the various economic sectors to the national budget; to show the budget allocations for defense, investment, administration, and consumption as proportions of sector and total national output; and to appraise the adequacy of budgetary resources for investment requirements under the First Five Year Plan (1953-57) of Communist China. For these purposes, the budgets of Communist China are described as to general features and accounting practices, and the final national budget for 1954 is analyzed in detail, comparisons being made with the budgets of previous years and with the planned budget for 1955. Budgetary trends are reviewed in relation to economic growth, and the estimated available budgetary resources are analyzed in relation to the needs for investment funds necessary to accomplish the Five Year Plan for economic development through 1957.

The information used in this report includes the annual budget reports of the Ministers of Finance for the years 1950-55, other commentaries of Chinese Communist officials and government organs concerning budgetary plans and results, official announcements of tax and control regulations and of results of production and trading operations of government and private organizations, a budgetary accounting handbook used in training students in national budget accounting, reports of refugees and repatriates from Communist China, and analyses of the gross national product of Communist China that have previously been completed in CIA.

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MOBILIZATION AND ALLOCATION OF RESOURCES
THROUGH THE NATIONAL BUDGET OF COMMUNIST CHINA*
1950-55

Summary and Conclusions

The rapid growth of the national budget of Communist China reflects the drive of the state toward the industrialization and modernization of the Chinese economy. The planned budget for 1955, almost 30 billion yuan (\$12.7 billion at the official exchange rate**), is more than four times greater than the budget for 1950. In relation to the gross national product (GNP), the budget has risen from about 16 percent in 1950 to 31 percent in 1955. Expenditures and receipts of the budget will continue to rise in the future but at a declining rate as the sources of nonrecurring receipts, largely a product of socialization, are exhausted.

The budget provided over 75 percent of the financing for investment purposes in 1955. Of the resources allocated in the budget, about 50 percent went to economic construction, and the defense sector obtained about 25 percent. Within the category of economic construction, heavy industry and rail transport are the chief recipients of funds. This pattern of investment reflects the allocation of economic construction funds under the Five Year Plan of Communist China. Achievement of the Five Year Plan investment program is largely dependent upon the ability of the state to obtain adequate funds through the budget.

Budget revenues are obtained chiefly from taxes and from the profits of state enterprises. Inasmuch as agricultural taxes, including industrial and commercial taxes on goods purchased by peasants, contribute 28.7 percent of the budget revenues, agricultural income still remains a major source of tax revenue. A large and growing share of national income and of budget revenue originates in those sectors of the economy controlled by budget allocations. The

* The estimates and conclusions contained in this report represent the best judgment of ORR as of 1 March 1956.

** The exchange rate used in this report is 2.367 yuan to 1 US dollar.

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planned increases in production in all sectors of the economy during 1956-57 will provide the necessary revenue for the investment goals of the Five Year Plan and other estimated budget expenditures.

The national budget of Communist China is used by the state as a major instrument in the achievement of the basic goals of the regime -- industrialization, modernization of defense, and socialization of the economy. State control over the allocation of resources, which is essential for the fulfillment of the program, is achieved by directly allocating resources in the state-owned sectors of the economy and by an indirect exercise of controls over the remainder of the economy through the application of rigid fiscal and monetary policies.

I. Introduction.

The national budget of Communist China is a consolidated cash account which includes the revenue and disbursements of all levels of government and the profits and investment expenditures of all state industrial enterprises.* The Minister of Finance gives an annual report on the budget, consisting of the final budget of the previous year and the planned budget of the current fiscal year. The fiscal year usually is well under way when the budget report is issued, as in 1955 when the Minister of Finance, Li Hsien-nien, reported on the budget in July. The budget reports give totals for five general categories of revenue and expenditures, with little or no descriptive detail about the accounts from which the larger categories are constituted. The official budget accounting manual (which was published in 1952 for the training of Chinese Communist students), however, contains a description of the items constituting

* The working capital requirements of state enterprises are the dual responsibility of the budget and the state bank. This responsibility has been divided as follows: industrial enterprises get most of their working capital through the budget, only borrowing from the state bank for seasonal or emergency needs, whereas commercial enterprises borrow the bulk of their working capital from the state bank and receive only minor portions through the budget. The state bank loans are not reflected in the budget. 1/ (For serially numbered source references, see Appendix D.)

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the major categories and provides, along with scattered information from other sources, sufficient basis for analyzing the accounts. ^{2/} The major revenue categories include taxes (agricultural, industrial, commercial, and other); profits and depreciation reserve funds of state enterprises; credits, loans, and insurance; the category other; and surplus carried forward. The major expenditure categories include economic construction; defense; social, cultural, and educational; administration; credit, loans, insurance; and the category other. Another expenditure category entitled capital construction was given for the first time in the 1955 budget report. The category capital construction covers expenditures for fixed assets under economic construction; social, cultural, and educational; and administration.

A. General.

Certain outstanding characteristics of the Chinese Communist budget, particularly as to revenue, differentiate it from the national budgets of private enterprise economies. Chief among such peculiarities in the revenue accounts is the revenue derived from profits and depreciation reserve funds of state enterprises, which constituted as much as 38.7 percent of 1954 budget receipts. The much smaller receipts of fees and charges of budget-supported hospitals, schools, and other welfare institutions are another type of revenue. Another such item, of significance in the past, was the very considerable revenue derived by the government in 1950 from the liquidation of some of the assets taken over from the Nationalist (Kuomintang) government. Only those assets in excess of quotas specified for particular enterprises were liquidated, and the receipts therefrom were entered in the budget under the category of other revenue. When the sale or assignment was made to a state enterprise, the value of the asset appeared as an expenditure.* ^{3/} Other revenue based on existing capital assets arose in 1951 when the assets of state enterprises were revalued. The increments in value were listed both as receipts and as an investment expenditure. ^{4/} To be noted also is the government's revenue from arbitrary tax penalties, confiscations, and "labor reform" (forced labor) camps -- receipts to be found only in a totalitarian economy. Finally, the

* There is a possibility that certain of these confiscated assets were not marketable and so have not been a source of receipts. Their estimated value may be listed as part of the surplus, accounting for surplus figures exceeding the actual budget results.

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handling of loan funds through the budget, although not arising necessarily from the socialization process in the Chinese Communist economy, is different from that in Free World countries. For example, producer and credit cooperatives and other semisocialist groups are provided some of their working capital in the form of loans which are allocated through the budget and which, when repaid, are listed as new revenue. This practice tends to inflate the accounts. 5/

The accounts are also inflated by the receipts and repayments of government foreign and domestic loans, which are included in the budget of Communist China. Such borrowing has resulted in the mobilization of resources to the extent of at least 2 billion yuan (\$845 million at the official exchange rate*) for the development program of Communist China since 1950.

Because the Chinese Communist budgets have been several times larger than any Nationalist Chinese budget, they have elicited both amazement and suspicion among Western observers. Even when adjustments were made for the addition of Manchuria as a taxable area, for the inclusion in the consolidated national budget of all local receipts from the hsien (county) level up, and for the enlarged sphere of government activity, there was doubt that the level of output in Communist China could support such budgets. The numerous forecasts of financial chaos in Communist China have not been borne out, however, for budget revenues have continued at a high level, and the general price level has been relatively stabilized since 1952.

Among the reasons advanced by Western observers for forecasting financial collapse has been the amount of nonrecurring revenue in the Chinese Communist budgets. Each year a new device has been used to absorb private capital, such as confiscation of enemy property, socialization of private enterprise, fines from the "Five Anti" campaign,** "contributions" in support of the Korean War, and, more recently, economic construction bond drives. The belief that such exhaustion of private assets is having an impact on the budget is supported by a new approach that has recently been taken to maintain financial stability -- the economy drive of 1955.

* Unless otherwise specified, all dollar values in this report are in terms of US dollars. The exchange rate used in this report is 2.367 yuan to 1 US dollar.

** A campaign of capital levies against alleged tax evaders and profiteers among private traders and investors.

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Save-food campaigns, elimination of "nonproductive" investment, administrative staff cuts, and -- even more significant -- across-the-board cuts in basic construction expenditures have been instituted, indicating at least a very tight revenue situation. Additional evidence that financial stringency may be of increasing urgency is the deficit on current account and the small revenue increase planned for 1955. Planned expenditures exceed planned current revenue for the first time since 1950. The rate of increase in planned receipts is less than in any previous budget and just matches the planned rate of increase in gross industrial and agricultural production.

Increased use of money taxes by the Chinese Communists is another change from the past. As a result of the grain-purchase program beginning in late 1953, even peasants are now receiving substantial parts of their incomes in cash, and their market purchases cause commodity and turnover taxes ostensibly to assume the dominant rank formerly occupied by the grain tax in the budget tax receipts. The monetary value of grain taxes, however, is a point of some obscurity insofar as budget figures are concerned, as official statements have placed grain taxes at varying proportions of the crop. Announcements of the volume of grain taxes, when related to the budget, indicate that the tax grain is carried at a low price which distorts the monetary value of the taxes.

Another apparent inconsistency of budget reports of Communist China is the claim of annual balance between receipts and expenditures. When Po I-po was Minister of Finance, until 1954 the previous year's surplus in each report was included with current receipts, giving the appearance of annual surpluses from 1950 on. Later, revised budget reports for previous years show a deficit in 1950 and a surplus from then on. Western analysts have found it difficult to accept the surplus claimed in 1951, when 1 million Chinese troops were fighting in Korea. The explanation appears to lie in the probability that some of the receipts from the 1952 "Five Anti" campaign were put back into the 1951 budget. This would be contrary to the Chinese Communists' officially stated accounting practice as set forth in their budget manual which requires that the budget be on a cash basis, closing on 31 December of each year. It is apparent, however, that the whole budgeting process runs behind schedule and that subordinate units avoid reporting until budget plans are fulfilled.

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Questions have also been raised as to the actual level of defense expenditures, a matter which will be discussed below in connection with the allocation of resources.

Finally, the Chinese Communists have shown some astuteness in devising ways of maintaining production and revenue despite the threat to incentives which is implicit in the heavy tax burden. The principal device in maintaining revenues at the required level has been to use standard yield and normal income in computing grain and income taxes. Thus the government decides what a certain grade of land should produce or the income that a firm or peddler should make and assesses the tax on the postulated rather than on the actual income.

B. Budget in Relation to the State Bank* Loan Program.

Of particular interest in connection with budgetary control and the size of the budget is the loan program of the state bank. As suggested above, budget policy really shapes the program of the state bank, the second most important means of resource control. This is borne out by the fact that budget funds make up 85 percent of the state bank deposits, part of the balance being in the form of private savings, which amounted to 1.63 billion yuan in 1954. Under the present division of responsibility, the state bank uses 80 percent of its funds to provide loans of working capital to state and cooperative commerce. 6/ The bulk of working capital of state and cooperative industry is provided directly through the budget. Agricultural loans are a divided responsibility, with the state bank (the agricultural bank since 1955) playing the major role. Recent budget speeches have made clear that use of so-called surplus funds for other than planned purposes or failure to build up a current budget surplus interferes drastically with the state bank's loan program.

The annual development plans of state enterprises include requirements for credit, and, in accordance with these approved control plans, bank loans are used to supplement the budgetary allocations. The state bank, in executing its supervisory responsibility for enforcement of the budget plan through monetary and credit controls, requires the various government organs and enterprises to submit in advance their plans for receipts and expenditures of funds during ensuing quarterly periods of the entire fiscal year. Cash receipts must be deposited daily in government

* All references to the state bank in this report are to the People's Bank of China.

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banks, and expenditure requirements must be planned and approved in advance. The bank sees to it that transactions are in accord with the budget plan, including provision for credit requirements, which must be planned and approved in advance and can be granted only by the state banks.

In addition to regulation by the budget and the banking system, other administrative controls, which cannot be readily reduced to value terms, are used by the Chinese Communists. Price controls, forced savings, forced procurement of agricultural goods at fixed prices, rationing, and other measures are essential parts of the Chinese Communist programs for industrialization and socialization.

C. General Trends in Budgetary Receipts and Expenditures, 1950-55.

The Chinese Communist planned budget of 1955 reached new heights in both revenue and expenditures. Planned current receipts of 28 billion yuan were 6.91 percent higher than in 1954 and roughly 31 percent of the Chinese Communist GNP. Inclusion of the surplus carried over from 1954 raises total revenue to 31.2 billion yuan.

Despite a rise in expenditures of 20.7 percent -- to 29.7 billion yuan -- 1955 was the fifth successive year in which a budget surplus was planned; this, however, was to be achieved by offsetting a deficit on current account by revenue from the surplus brought forward. The summarized annual budgets of Communist China, showing categories of revenue and expenditures by amount, by percentage of total, and by sector for 1950-55, are shown in Tables 1 and 2.*

The annual budget reports of Communist China present revenue receipts in two ways, according to form of ownership and type of revenue. Profits, depreciation reserves, and taxes of state enterprises have always been the largest source of receipts by sector and between 1950 and 1955 have risen from 34 to 69 percent of receipts. Among the various types of revenue, total tax payments take first place. The proportionate share of taxes, however, is**

* Tables 1 and 2 follow on pp. 8 and 9, respectively.

** Continued on p. 10.

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Table 1

Communist China: Budget Revenue and Expenditures
1950-55

Revenue a/ Expenditures	1950		1951		1952		1953		1954		1955 Plan	
	Million Yuan	Percent of Total	Million Yuan	Percent of Total	Million Yuan	Percent of Total	Million Yuan	Percent of Total	Million Yuan	Percent of Total	Million Yuan	Percent of Total
Taxes	4,897.81	75	8,112.17	62.5	9,768.45	55.5	11,967.12	55	13,218.08	50	13,780.57	49
Profits of state enterprise	869.65	13	3,053.73	23.5	5,727.97	32.5	7,669.05	35	9,961.50	38	11,115.81	40
Credits, loans and insurance	327.91	5	567.95	4.5	193.16	1	491.83	2.5	2,345.37	9	3,153.40	11
Other	423.75	7	1,233.17	9.5	1,870.10	11	1,634.36	7.5	711.87	3		
Subtotal	6,519.12	100	12,967.02	100.0	17,559.68	100.0	21,762.36	100.0	26,236.83	100	28,049.78	100
Surplus (carried over from previous year)									4,509.00 b/		3,142.74	
Total									30,745.83		31,192.52	
Expenditures												
Economic construction	1,735.37	25.5	3,511.15	29.5	7,626.34	45	8,644.53	40	12,358.22	50	14,188.76	48
Social, cultural, and educational	755.01	11	1,343.76	11	2,279.68	13.5	3,360.69	15.5	3,460.51	14	3,850.69	11
Defense	2,827.39	41.5	5,060.81	42.5	4,371.34	26	5,679.22	26.5	5,813.53	24	7,193.15	24
Administration	1,313.27	19	1,744.86	15	1,727.38	10	2,118.69	10	2,162.07	9	2,241.56	7.5
Other	177.02	3	241.61	2	782.28	6	1,684.65	8	838.11	3	2,262.56	9.5
Total	6,808.06	100.0	11,902.19	100.0	16,787.02	100.0	21,487.78	100.0	24,632.44	100	29,736.72	100.0
Surplus or deficit	-288.94		1,064.83		772.66		274.58		1,604.39		-1,686.94	

a. See Table 2, p. 9, below, for breakdown according to sector.

b. The budget speech gives this figure as the surplus funds accumulated since 1949. There is no official explanation of the fact that the announced surplus exceeds the unspent revenue for those years by 1,081.48 million yuan. The 1955 budget speech states that roughly half of the surplus had been previously allocated, and so only 3,142.74 million yuan is carried over into the 1955 budget.

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Table 2
Communist China: Budget Revenue, by Sector
1950-55

Sector	1950		1951		1952		1953		1954		1955 Plan	
	Million Yuan	Percent of Total	Million Yuan	Percent of Total	Million Yuan	Percent of Total	Million Yuan	Percent of Total	Million Yuan	Percent of Total	Million Yuan	Percent of Total
Taxes, profits and depreciation reserves of state enterprises	2,221.72	34	6,399.22	49	10,181.10	58	13,623.24	62.5	16,344.79	65	18,618.60	69
Taxes and bond payments by co- operatives					189.64	1	539.71	2.5	914.44	4	1,282.65	5
peasants	1,931.61	30	2,356.11	18	2,809.55	16	2,933.57	13.5	3,565.09	14	3,162.58	12
Taxes and bond payments by pri- vate enterprises	2,146.09	33	3,716.35	29	3,720.90	21	3,703.95	17	3,342.11	13	2,877.22	11
Taxes and bond payments by joint enterprises	219.69	3	495.75	4	184.37	1	267.68	1.2	415.88	1.5	532.42	2
Other					474.12	3	694.39	3.3	476.01	2	354.95	1
Total	6,519.12	100	12,967.02	100	17,559.68	100	21,762.36	100.0	25,053.33	100.0	26,889.95	100

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declining, and the profits and depreciation reserves of state enterprises are a rising proportion. As percentages of total revenue, taxes fell from 75 percent of 1950 receipts to 49 percent of planned 1955 receipts, and the profits and depreciation reserves of state enterprises rose from 13 percent to 40 percent of receipts during the same period.

Credits, loans, insurance, and the category other are the remaining types of revenue. A notable increase in these categories was explained in the 1955 budget speech as being caused principally by an increase in Soviet military credit. The elements comprising these categories and other types of revenue are analyzed in some detail below.

Expenditure categories of the Chinese Communist budget are economic construction; defense; social, cultural, and educational; administration; and the category other, arranged in order of magnitude in the 1954 and 1955 budgets. Capital construction expenditures were also given, and these serve as a good measure of fixed investment from year to year in Communist China. Most of the capital construction funds come under the allocation for economic construction, although some involve the administration and the social, cultural, and educational categories.

A small decline in the proportionate share of economic construction expenditures is planned for 1955, for which a rise in defense spending probably is responsible. These two categories appear to be competitive and have more or less exchanged positions over the years. Defense spending took up 40 percent of the 1950 and 1951 budgets and dropped to its present level of roughly 25 percent in 1952. The reverse trend occurred in economic construction, which rose from 25 percent in 1950 to the present level of about 50 percent, the rise occurring principally in 1952.

Within the economic construction category, heavy industry and rail transport have been consistently accorded the greatest share of expenditures. This emphasis in allocation of resources was intensified in the 1955 budget, which apportioned over 50 percent of economic construction funds to these two sectors. The largest producers of national income, agriculture and light industry, receive only a minor share of economic construction funds. Of the 4.4 percent allocated in 1955 to agriculture, forestry, and water conservancy, almost all is for flood control.

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The Communists have succeeded in holding down the share of administrative expenditures, thus freeing a greater portion of revenue for other more productive uses. Administrative expenditures have steadily declined proportionately from 19 percent of the 1950 budget to 7.5 percent of the 1955 planned budget.

Although the Chinese Communists devote much propaganda to the peaceful nature of their budget and to their expenditures for welfare purposes, as a proportion of the total budget the annual allocations for social, cultural, and educational activities have in fact remained fairly constant at about 13 percent.

Recent budgets have been drawn up to provide a general reserve fund, 7/ which would allow some latitude for shifting expenditure allocations during the fiscal year and for tiding over the seasonal periods of low receipts of revenue during the year. Planned budgets since 1953 have contained appropriations to such a reserve fund, but no final budget has indicated that such a reserve fund was in fact achieved.

Finally, as to trends in budget fulfillment, there has been a consistent underestimate of revenue and overestimate of expenditures. Profits of state enterprises seem to be the most unpredictable revenue category for the Chinese Communist planners, although an unexpected Soviet loan in 1954 caused the greatest single case of overfulfillment of planned receipts. On the other hand, failure to carry out planned investment in capital construction reflects a serious shortcoming in Chinese Communist planning, in contrast to which there has been regular overspending on economic construction. This discrepancy may be partially explained by the fact that certain economic construction expenditures, such as those for geological surveys, and assignment of working capital and operating expenses to socialized enterprises are not dependent on scarce materials and equipment and so can be more readily carried out. Expenditure fulfillment by such measures may underlie recurring press reports of official criticism of wasteful and non-productive expenditures.

In summary, as budgetary controls have been extended and as socialized industry and commerce have expanded, budgetary receipts and allocations have also expanded, although the problem of achieving a carryover reserve fund appears to be still unsolved.

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D. Size of the National Budget in Relation to Output.

To give some perspective to budget magnitudes, total receipts are related to estimated GNP. This procedure is used with important qualifications. First, the budget and GNP are not comparable insofar as the budget includes receipts from other than current production, such as the sale of capital assets. In addition, budget receipts can be changed without any change in the extent of state control of the economy as would occur if the state enterprises retained their depreciation reserves or portions of profits for enterprise investment as in the USSR. Change in the proportion of output flowing through the budget cannot be equated to burden on the economy, because the allocation of the receipts is the important determinant and the government activities may have increased output by more than the increment of budget receipts. A comparison of the national budget with GNP shows the budget rising from 15 percent of GNP in 1950 to 30 percent in 1954.

A survey of budget operations over the past 5 years shows that resources mobilized by the government through the budget have been allocated primarily to defense and investment activities. Of total expenditures from 1950 to 1954, about 80 percent were devoted to these and other nonconsumption purposes.*

A comparison of GNP with total budget receipts shows a constant rise in the proportion of total budget receipts to GNP, as shown in Table 3.** This proportion probably will not rise so rapidly in the future, although the effect on budget receipts of the recent drive for joint state-private enterprise is not yet clear. If the state's share of profits greatly exceeds the former income tax on such earnings, there will be a substantial rise in the proportion of budget receipts to GNP.

* Total expenditures were 81.6 billion yuan. Nonconsumption expenditures totaling 68.3 billion yuan were defined as follows: 23.6 billion yuan for defense; 33.6 billion yuan for economic construction; and one-half the expenditures for administration and miscellaneous, or 11.1 billion yuan.

** Table 3 follows on p. 13.

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Table 3

Communist China: Relationship of the Budget
to Gross National Product
1950-55

Item	1950	1951	1952	1953	1954	1955 Plan
Gross national product a/ (by end use and in billion current yuan b/)	41.7	57.8	68.7	80.1	85.4	90.6
Percentage increase over preceding year		38.6	18.8	16.6	6.6	6.1
Budget (current receipts in billion current yuan)	6.5	12.96	17.56	21.76	26.2	28.05
Percentage increase over preceding year		99	35.5	24	20.4	7
Budget receipts as a proportion of GNP (percent)	15.5	22.4	25.5	27.2	30.7	31

a. 8/

b. The price index used for conversion to current yuan is as follows: 1950, 81; 1951, 87; 1952, 100; 1953, 108; 1954, 110; 1955, 110. 9/

II. Mobilization of Resources Through the National Budget.

A. General.

An over-all view of resource mobilization through the budget can be obtained by relating 1954 budget receipts to the income of various sectors, as drawn from an analysis of GNP in Communist China. 10/ For this purpose, the official Chinese breakdown of revenue by form of ownership (that is, tax and bond purchases of private enterprise) is used. This breakdown excludes estimated Soviet loans of 1,215 million yuan. The usual sector-of-origin distribution of GNP is adapted for comparison to the budget. The apportionment of income among agriculture, private nonagriculture, state enterprises, and indirect taxes is discussed in Appendix A.

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On a relative basis, private income is being very heavily taxed (see Table 4*), with 18 percent of agricultural income and 28 percent of private nonagricultural income collected by the state. The tax burden is such that private per capita disposable income, even in the nonagricultural sector, is barely at a subsistence level. Provision of 1 catty (1.3 pounds) of rice per day would absorb 65 percent of rural per capita disposable income of 72.5 yuan and about 30 percent of urban income of 159.4 yuan.

The relationship of the budget receipts of Communist China to sector income in 1954 is shown in Table 4.*

B. Taxes.

Although taxes remain the chief source of revenue in Communist China, the rapidly rising profits of state enterprises have reduced the relative proportion of tax revenue from 75 percent of total budget receipts in 1950 to 50 percent in 1954. At the same time, within the tax category there has been a shift of even greater magnitude -- away from reliance on agricultural taxes and in favor of industrial and commercial taxes. These changes, however, do not involve a corresponding shift in the tax burden, as the industrial and commercial taxes are covered mainly in the prices of consumer goods. Inasmuch as peasants are the chief consumers in China, agricultural income is still the major source of tax revenue.

1. Industrial and Commercial Taxes.

The principal types of industrial and commercial taxes are business turnover, commodity, and income taxes. State enterprises are exempt from the income tax because their profits are remitted to the state. There is no personal income tax on wages and salaries, although all forms of business income, such as interest and commissions, are subject to income tax. 11/

The determination of coverage and the setting of rates within the major tax categories have proved very effective means of drawing resources from certain sectors for use in others. The rate structures of the revised commodity and business turnover taxes bear witness to this fact, in that low rates apply to producer goods and essential consumer goods and high rates to luxury

* Table 4 follows on p. 15.

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Table 4

Communist China: Relationship of Budget Receipts to Sector Income
1954

Sector	Income <u>a/</u> (Billion Yuan)	Budget Receipts (Billion Yuan)	Proportion of Receipts to Income (Percent)	Proportion of Allocated Receipts <u>b/</u>
Agriculture, forestry, and fisheries	40.48	7.54 <u>c/</u>	18.6	28.2
Private nonagriculture	30.26	8.58 <u>d/</u>	28.3	32.1
State enterprises less wages <u>e/</u>	9.97	9.97 <u>f/</u>	100	37.3
Indirect taxes		0.60 <u>g/</u>		2.4
Indirect taxes	5.98			
Total	<u>86.69</u>	<u>26.69</u> <u>h/</u>		<u>100.0</u>

a. See Appendix B for an explanation of income estimate.

b. Estimated Soviet loans of 1,215 million yuan were not allocated.

c. The value of peasant taxes and bonds is given in the budget as 3,565 million yuan. The balance of 3,975 million yuan is imputed or shifted from other sectors.

d. This total is the sum of the following: income taxes, 2,982 million yuan; indirect taxes, 4,270 million yuan; other taxes, 323 million yuan; bonds, 548.4 million yuan; insurance, 97 million yuan; and other revenue, 356 million yuan.

e. Income of state enterprises is 17 billion yuan. Wages of 7.03 billion yuan are subtracted from this and included in private nonagriculture income.

f. Given in 1955 budget as profits and depreciation reserves of state enterprises.

g. Some of the indirect taxes are on producer goods sold among state enterprises.

h. The relationship of this total to budget receipts of 26,236 million yuan is as follows: Soviet loans of 1,215 million yuan are excluded, and receipts of 1,658 million yuan were imputed (see peasant taxes), giving surplus receipts of 443 million yuan.

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items. A clear example of allocation of resources by the tax system was the setting of a 9-percent rate on cloth made from native yarn and a 5-percent rate on cloth made from machine-made yarn, the purpose being to foster the modern sector of an industry beset with shortages of raw materials.

The revision of these taxes (effective 1 January 1953) effected a regrouping of commodities subject to the old commodity tax and to the business turnover tax into the following two groups: one group to be subject to a new commodity circulation tax and the other group to be subject to a new commodity tax. Table 5* shows the revised tax schedules for the two groups of commodities. The rates listed for the revised taxes are given as a proportion of the final selling price rather than the actual rate.

Many of these taxes and rates were in effect before 1949, but the tax burden is believed to be heavier now because of the improved methods of collection and the stern measures taken against evasion.

The income tax, which contributes about 20 percent of industrial and commercial tax revenues, must be paid by all private industrial and commercial enterprises, with rates ranging from 5 to 30 percent of net income. The average rate is about 25 percent. 12/ Business incomes under 300 yuan are exempt. Incomes over 10,000 yuan are subject to the maximum rate of 30 percent. Within this range there are 21 tax classes.

There are a number of ways in which the income tax contributes to the withdrawal of resources from "undesirable" areas into favored fields. The favored industries, such as steel and chemicals, may deduct from 30 to 40 percent of net profits for tax purposes. Further discrimination is possible by the arbitrary use of estimated rather than actual income for tax purposes and by demands against some firms for advance payment of taxes. Both of these devices have been used inequitably to hamper and in some cases to eliminate private enterprise.

The granting of income tax exemption to cooperatives during the first 3 years of their existence was designed to encourage the growth of cooperatives. This privilege was suspended in 1953

* Table 5 follows on p. 17.

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Table 5
Communist China: Revised Industrial and Commercial Tax Structure of 1 January 1953
Compared with That of 1949-50

ase 2000/04/17 : CIA-RDP79-01093A001

Tax	Number of Categories	Description	Revised Tax	Taxes Still Applicable (Percent)				Stamp: Three Levels
				Commodity	Business Turnover			
					Industrial	Wholesale	Retail	
Group I: commodity circulation tax	22	New tax replaced the old commodity tax, the business turnover tax at three levels, and the stamp tax at three levels	5 to 66 percent of final selling price					
Group II: new commodity tax a/	37	New tax replaced the old commodity tax, the industrial business turnover tax, and the stamp tax	2 to 50 percent of wholesale price		1.15 to 3.45	1.15 to 3.45		0.6
Group III: old commodity tax a/	24 (Some categories split by the revision)	Multiple taxation	3 to 120 percent applied to wholesale price	1.15 to 3.45	1.15 to 3.45	1.15 to 3.45		0.9

ase 2000/04/17 : CIA-RDP79-01093A001

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at about the same time that price subsidization of cooperatives was eliminated, indicating that the need for tax revenues superseded the usefulness of cooperative competition as a means of eliminating private enterprise. 14/

Income taxes will continue to decline as the private share of the economy diminishes. The profits of the remaining private enterprises will be small, as is the bulk of manufacturing and sales, and will be under state contracts on a commission basis, which barely covers costs.

2. Other Taxes.

Certain tax receipts are unaccounted for in the most recent budget speeches. Two possible alternative explanations of the residual sum are separate listing of salt taxes or separate treatment of certain locally retained taxes. The latter interpretation is considered more likely, as local taxes on real estate, land deeds, and licenses could appropriately be distinguished from industrial and commercial taxes.

3. Budget Burden on the Peasants.

In respect to the burden imposed on the peasants by the Chinese Communist system of resource mobilization, previous analyses have stressed that the officially reported agricultural taxes are not a fair measure of the true tax burden on the peasant. Among the various ways in which receipts are obtained from the peasant over and above the listed value of grain taxes are those mentioned below.

The value at which agricultural taxes-in-kind are listed in the budget is 20 percent lower than the price at which the grain is valued as an expenditure.* 15/ The Ministry of Food distributes tax grain to other ministries for wage payments, and it probably lists the added value of the grain as part of its profits. Thus profits of state enterprises are swelled by part of peasant tax payments. In 1954, profits resulting from this paper markup would be approximately 7 percent of the profits and depreciation reserves of state enterprises.

* Forty billion catties (1 catty equals 1.3 pounds) of commercial grain were collected in 1954. Agricultural taxes were given as 3.277 billion yuan, or 0.0819 yuan per catty. Grain is listed at 0.1 yuan per catty.

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The forced sale of grain to the government has also been suggested as part of the true peasant tax burden. The farm purchase price is somewhat lower than the resale price, thus giving the government the benefit of the trade markup. In this respect it is clearly indicated by available prices that the difference between farm purchase prices and resale prices to the peasants is not very great and involves little, if any, monopoly gain. Although the state monopoly of the purchase and sale of major agricultural commodities gives to the state revenue that previously would have been private income, these socialized profits do not necessarily constitute an additional burden on the peasants. Only insofar as the grain-sale quota imposed on the peasant requires the noncustomary repurchase of such grain must the peasant pay for unwanted trade costs and profits.

Local governments impose their own levies on the peasants over and above ordinary local taxes listed in the consolidated budget. Although these local surcharges were supposed to have been abolished in 1952-53, there are indications that the local surcharges still remain. These surcharges are estimated to raise grain taxes as much as 25 percent. In addition, the peasants pay taxes on other agricultural crops, such as tea, cotton, and tobacco, and at least 25 percent of the total commodity taxes.

The peasants also contribute revenue to the government in the form of credit, which in effect is extended through forced bond purchases and by the forced sale of grain on credit or in exchange for savings certificates. In summary, it is estimated that these combined levies raise the tax burden on the peasant by more than double the amount of the listed grain taxes.

Table 6* shows the tax burden on the peasants as compared with agricultural income in 1954.

C. Profits and Depreciation Reserves of State Enterprises.

The Chinese Communists are fond of emphasizing the growth in the budget category profits of state enterprises as proof of the superior productivity of a socialist economy. They point to the

* Table 6 follows on p. 20.

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Table 6

Communist China: Estimated Tax Burden on Peasants
1954

Item	Million Yuan	Million Yuan	Percent
Grain taxes	4,116.55 a/		
Bond purchases	287.6 b/		
Insurance and other	553 c/		
Commodity taxes	1,762.0 d/		
Local surcharges	819 e/		
Total tax		7,538.15	
Farm income		40,480.0	
Proportion of agricultural taxes to income			18.6
Proportion of agricultural taxes to budget revenue			28.7 f/

a. This figure reflects an adjustment of announced grain taxes based on 1952 farm income and taxes. The statement of the value of farm income in the Five Year Plan was related to an announcement that food crop taxes were 7 percent of farm income. 16/ As food crops represent only 77 percent of major crops subject to grain tax, the tax on commercial crops was added on the assumption that taxes are in proportion to production. The resulting value of agricultural taxes was 57 percent higher than the budget figure. Only 80 percent of the adjusted grain tax was listed, as farm income figures have been adjusted to eliminate the overstatement, arising from the valuing of all farm output at prices above farm procurement prices.

b. Given in the 1954 budget.

c. The peasants are estimated to pay two-thirds of insurance premiums, or 197 million yuan, 17/ and half of other receipts, or 356 million yuan.

d. Cash purchases by the farmer are estimated to be 14 billion yuan and the average commodity tax rate on rural purchases to be 8 percent. The tax rate is derived from a weighting of commodity tax rates to an estimated rural pattern of expenditures. Other taxes

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Table 6

Communist China: Estimated Tax Burden on Peasants
1954
(Continued)

on property raise this total by 646 million yuan.

e. Twenty-five percent of announced grain taxes.

f. This percentage would be 27 percent if imputed taxes were added to reported budget revenue.

large increase in such revenue -- from 869 million yuan in 1950 to 3 billion yuan in 1951 and yearly increases of approximately 2 billion yuan thereafter -- as support for their theme. The official statements often give credit to socialist industry for these increases, leaving open the question of whether the increases result more from the nationalization of the private sector and more intensified utilization of existing capacity than from increased production of expanded or newly constructed state enterprises.

An analysis of the factors underlying the growth of the category profits of state enterprises is important not only because it relates directly to the achieved rate of growth of the state sectors of industry and trade but also because it provides a basis for judgment of the extent to which the Chinese Communists can depend on increases of revenue of the same magnitude in the future.

In order to measure the extent to which the rise has been due to enlarging the base by the confiscation of private production, several assumptions were made. It was assumed that former private enterprises are contributing the same proportion of output which they contributed as private enterprises. This implies no change in relative productivity or profit margins. Profits on that proportion of output by which private industry and trade have declined since 1949 were considered the fruits of socialization. This approach supported the conclusion that the combined socialization of trade and industry is the basis of 43 percent of profits and depreciation reserves in the 1954 budget.

The calculations underlying this conclusion were as follows. Private industry (including all cooperative and half of joint

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state-private enterprises) declined from 65 percent of industrial output (excluding individual handicrafts) in 1949 18/ to 30 percent of output in 1954. 19/ Profits on the 35 percent of output from the socialized sector constituted 23 percent of profits and depreciation reserves in 1954.*

Private trade declined from roughly 81 percent of trade in 1950 21/ to 50 percent in 1954. 22/ Profits on the nationalized proportion in 1954 were equal to 20 percent of profits and depreciation reserves.

The goals for further socialization in the Five Year Plan will affect, for the most part, industrial profits, as private commerce will not be taken over directly by the state. Private industrial output, including one-half of joint state-private production, is to decline to 28 percent of the total by 1957, according to the Five Year Plan, so that the profits and depreciation reserves category of the budget will continue to be bolstered by socialization gains. It is obvious, however, that this method of securing revenue has certain absolute limits, which are, in fact, already reflected in the declining rate of increase of profit revenue in the 1955 planned budget. The 1955 planned increase of only 1 billion yuan in profits receipts (compared with the earlier annual increase of 2 billion yuan) is believed to be symptomatic of the declining rate of increase in this category through the remaining years of the Five Year Plan, although this decline may be delayed until 1956 because of the unexpected great expansion in the number of joint state-private enterprises in late 1955. The profits derived from the state's share of the enforced joint operation probably will more than compensate for the loss of income from tax receipts.

There has been considerable speculation as to the portion of state profits which arises from state trade in grain and in general from its monopoly over the sale of major agricultural commodities (as distinct from its revenue from agricultural taxes-in-kind and indirect taxes). The best information available pertains to pricing and volume of state grain trade. This information indicates that roughly 15 percent of state enterprise profits arise in grain trade. State sales of grain in 1954 totaled about 44.6 million

* Profits are taken as 65 percent of value added by industry and 60 percent of value added by trade, excluding indirect taxes as found in the analysis of the Chinese Communist GNP. 20/

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metric tons. ^{23/} Average profit per ton is estimated to be 30 yuan, yielding state grain profits of 1.4 billion yuan.

It is estimated that trade in other agricultural commodities raises the proportion of state enterprise profits directly dependent on agricultural commodities to a total of roughly 25 percent.* With a decline in state grain sales planned by 1957 and the major gains already wrested from monopoly sales of agricultural commodities, the conclusion that yearly increases in profits revenue will level off after 1955 or 1956 at 1 billion yuan is substantiated.

By relating the profits of state enterprises as shown in the 1954 budget to the profits' share of value added in production and services, it is possible to derive an estimated breakdown of the budget revenue category profits and depreciation reserves of state enterprises. This comparison indicates that the state obtains the largest proportion of its profits from industrial enterprises. Within the industrial sector, heavy and light industry contribute about an equal amount of profits revenue, despite the very much smaller share of light industry in investment allocations. Table 7** shows the estimated distribution of the category profits and depreciation reserves of state enterprises, by sector.

D. Credit, Loans, and Insurance.

Soviet credit and national bond campaigns are the major items in this category. That portion of the category ascribable to Soviet credit became of great importance in 1954 when unanticipated Soviet loans were indicated as a partial explanation for a 91-percent overfulfillment of planned receipts. When subtractions are made for all other items in the category, an unplanned loan of from 945 million yuan to 1,183 million yuan is indicated. No mention of a loan of this magnitude appeared in the press, and it has been interpreted as covering secret military deliveries by the USSR during 1954. Credit of the same magnitude for further military supplies, including those turned over at Port Arthur, is shown in the planned budget for 1955.

* The more general subject of the agricultural versus nonagricultural origin of budget revenue is discussed in greater detail in IV, A, below, where a breakdown of all budget receipts is made as an aid to weighing the impact on the budget of possible failure to meet certain production targets of the Five Year Plan.

** Table 7 follows on p. 24.

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Table 7

Communist China: Estimated Breakdown of the Budget Category Profits and Depreciation Reserves of State Enterprises, by Sector
1954

Sector	Proportion of Sector Owned by State (Percent)	Profits a/ (Million Yuan)	Proportion of Total Profits Category (Percent)
Industry	65 b/	4,185	42
Heavy	90	1,060	
Light	50	1,044	
Engineering	70	620	
Coal	80	510	
Electric power	80	690	
Petroleum	100	261	
Trade and distribution	50 c/	3,164	32
Transport and telecommunications	80 d/	926	9
Construction	90 d/	1,687	17
Total		9,962	100

a. Total profits were derived from value-added indexes based on physical production (1952 = 100) adjusted for an 8-percent price rise in 19, over 1952. Profits were assumed to be varying proportions of value added in industry, the average being 65 percent; for trade and construction, 60 percent; and for transport and telecommunications, 55 percent. The proportion belonging to the state was applied to total profits.

b. This proportion includes 59 percent from state and 6 percent from the state's half share in the joint enterprises. State ownership of particular industries is based on scattered announcements and in some cases is interpolated from data in the Five Year Plan.

c. This proportion is derived from announced state ownership of wholesale and retail trade. The rate was applied to the value added strictly by trade and excluded native transport.

d. Estimated.

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There was a considerable amount of revenue unaccounted for in the 1951 and 1953 budgets which also may have reflected secret military deliveries or short-term credits on foreign trade accounts. There was no significant amount of revenue unaccounted for in the 1952 budget, which may be explained by the fact that foreign exchange assets seized in the "Five Anti" campaign were sufficient to meet the normal import surplus from the Soviet Bloc.

The inclusion of bond receipts as ordinary revenue is a feature of Chinese Communist budgets. There have been 3 nationwide bond campaigns up to the present time, with sales ranging from 286 million yuan in 1950 to over 900 million yuan in 1954. The 1955 subscription campaign, the announced goal of which was 600 million yuan, probably will be oversubscribed also, following the pattern set in 1954. Whereas regional quotas were used in 1950, the 1954 and 1955 drives assigned quotas to specific sectors. The workers' quota was raised to 25 percent in 1955, but private enterprise still has the major assignment of 50 percent. Peasants have been the most reluctant purchasers, but the enlarged forced grain sales program gives the state greater control over their income.

The bond-redemption schedule has been extended steadily from 5 years for the 1950 bonds to 10 years for the 1955 bonds. Each year a certain percentage of each bond issue is retired by lot. Interest rates on the bonds have dropped from 5 percent in previous years to 4 percent in the 1954 and 1955 issues.

The nature of the insurance receipts is not clear, as the profits of the compulsory insurance system established in 1951 are included in the category of profits of state enterprises. It is believed that these receipts may be the reserves of the insurance company which the state assigns as working capital to other enterprises. This is borne out by a press comment on the insurance plan which indicated that China could benefit by the Soviet experience with this very fertile source of working capital. 24/

An estimated breakdown of 1954 receipts under this category is given in Table 8.*

* Table 8 follows on p. 26.

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Table 8

Communist China: Estimated Breakdown of the Budget Category
Credit, Loans, and Insurance Receipts
1954

Million Yuan	
Item	Amount
Bond sales	836 <u>a/</u>
Soviet loans	1,215 <u>b/</u>
Insurance (residual)	294
Total	<u>2,345</u>

a. 25/

b. Based on 142 million yuan under the 1950 loan agreement and 1,073 million yuan in estimated 1954 loans.

E. Other Revenue.

The intermittent character of most of the receipts under the category other is reflected in sharp changes in absolute collections. It is the one category in which revenue has not increased steadily.

The types of receipts included in this catch-all category are donations, confiscated assets, currency issue, revenue from forced labor camps, and operating revenue of budget-financed enterprises. Early budget reports given by Finance Minister Po I-po included the surplus carried over from previous years in this category. This practice was discontinued in the 1955 budget report, which lists as revenue only that portion of the surplus that is specifically appropriated and clearly distinguishes this portion from current receipts. The reasons for the separation and disposition of the accumulated surplus are discussed below.

Two items of other revenue -- donations and confiscated assets -- appear to substitute for bond drives when ordinary revenue sources are exhausted. Donations in support of the Korean War of approximately 500 million yuan played an important role in balancing the 1951 budget. Extraction of this sum required rather stringent

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measures not usually associated with the concept of donations. The following year, extraordinary receipts were secured under the guise of the "Five Anti" campaign against tax evasion, excess profits, and other crimes. Penalties resulted in the turnover of all or part of the assets of a majority of private firms. The revenue from this virtual capital levy has been estimated to be as high as 10 billion yuan, but this appears excessive even if some of the confiscation is reflected elsewhere than in the category other. A more realistic estimate would be about 4.3 billion yuan, a figure reached by taking the unaccounted-for revenue in the category other for 1952 and 1951 (the "Five Anti" campaign was initiated in the Northeast region in 1951) and adding to it that portion of the surplus in excess of the 1950-53 budget balances. Another possibility is that some of the revenue from the "Five Anti" campaign did not come in until 1953. Revenue in the category other for 1953 is almost as much as in 1952 and is approximately 1 billion yuan higher than in 1954. There is no apparent explanation for the 1953 receipts, and, judging by the 1954 receipts, which are described as "devoid of certain special and temporary receipts," it is probable that 1 billion yuan of the 1953 revenue resulted from the "Five Anti" campaign.

Currency issue, admittedly, was used extensively in 1949 and 1950 because the state bank had insufficient reserves to support its loans to the government. ^{26/} Currency issue to meet expenditures in those years totaled at least 2.1 billion yuan, as provision is made in the 1955 budget to repay this much of the government's 1949-50 overdraft on the state bank. Currency issue apparently is no longer relied upon as a source of budget revenue, an achievement of great importance in maintaining price stability in Communist China.

Another item shedding light on the Chinese Communist policies is revenue from labor camps, which is listed on a gross basis. It is estimated that in 1954 gross receipts from income of these labor camps amounted to 150 million yuan. This figure is based on two other estimates -- one on the gross value of production per prisoner and the other on the number of persons in labor camps. In arriving at the estimate of gross revenue from prison labor, the value of output per capita was assumed to be one-half the per capita gross agricultural production, as statements by former prisoners indicate that labor productivity is relatively low in prisons. ^{27/} The number of persons in forced labor camps in Communist China has been

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variously estimated, with some estimates as high as 10 million persons. A figure of 2.8 million is used in this estimate because it approximates the total derived from camp studies.

The most sizable continuing type of receipts in the category other is the operating income of budget-financed enterprises. These receipts include tuition fees and movie-ticket sales.

There are two items under the category other which seem to be counterbalancing figures that cancel out in the consolidated national budget. Subsidies from higher levels of government to lower levels and transfers from lower levels to higher levels appear in subordinate level budgets as a receipt and again as an expenditure under the category other. The breakdown of the 1954 budget given in this report assumes that these are bookkeeping items and that they cancel out in the consolidated national budget. The estimated breakdown of the budget category other for 1954 is shown in Table 9.

Table 9

Communist China: Estimated Breakdown of the Budget Category Other
1954

Million Yuan	
Item	Amount
Administrative revenue	392 <u>a/</u>
Public property revenue (residual)	100
Armed forces production	70 <u>b/</u>
Labor camp revenue	150 <u>c/</u>
Total	<u>712</u>

a. Composed of 152 million yuan for theater tickets (760 million at 0.2 yuan); 50 million yuan for clinic and miscellaneous fees; and 190 million yuan for tuition fees (average tuition fee of 6 yuan paid by approximately 30 million students).

b. 28/

c. Estimate.

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F. Surplus Revenue.

The 1955 budget report of Communist China stated that the surplus was 6,113 million yuan at the end of 1954. It is not clear how this surplus was accumulated, for the unexpended balance from previous years' budgets totals only 3,427 million yuan. A possible explanation for the difference is that some of the assets confiscated during the "Five Anti" campaign were included in the 1954 total announced surplus but were not listed as current receipts under the category other. Such a division of the "Five Anti" campaign receipts is supported by the Budget Accounting Manual, which lists fines for tax violations and various specified offenses as an item in the revenue of the category other, but makes no provision for confiscation of excess profits or profits arising from poor-quality goods.

Certain statements in the 1955 budget report clarify the nature of the surplus category and indicate that it is for the most part fictitious. Its fictitiousness arises from the fact that all but 3,142 million yuan of the surplus was already obligated by the end of 1954. The available surplus is even lower if a 1955 appropriation of 1,687 million yuan to state enterprises for repayment of overdue loans from the state bank is considered as an existing obligation. Among the obligations met out of the accumulated surplus at the end of 1954 were retirement of part of a 1949-50 central government overdraft on the state bank; replenishment of local budget revolving funds; and exclusion from the surplus of certain special accounts in the state bank, the latter probably involving funds over which the government acts as trustee.

A clarification of the relationship of the state bank loan program to government surplus accounts was made necessary because of overlapping plans for use of the same funds. In both the 1953 and 1954 budget years, budget officials apparently drew on the surplus funds as planned, without due consideration of the state bank's deposits and reserves position, thus forcing the state bank to contract its loans of working capital to state enterprises and cooperatives. The state bank now has use of the funds repaid to it for loan purposes under the 1955 planned budget.

Table 10* shows the claimed surplus of the budget (6,113.4 million yuan). It is interesting to note that the deficit on current

* Table 10 follows on p. 30.

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account in the planned 1955 budget is equal to the allocation from surplus funds of 1,686.9 million yuan to state enterprises for repayment of overdue state bank loans.

Table 10

Communist China: Disposition of the Reported Surplus
Brought Forward in the Planned Budget of 1955

		Million Yuan
Item	Amount	
Repayment of 1949-50 government overdrafts on state bank		2,158.8
Transfer to special accounts in state bank		504.4
Replenishment of local governments' revolving funds		307.4
Allocated for 1955 planned budget expenditures:		
Repayment of state enterprises' loans from state bank	1,686.9	
Increase of local governments' revolving funds	85.1	
		<u>1,772.0</u>
Unallocated		1,370.8
Total		<u>6,113.4</u>

III. Allocation of Resources.

Modernization of the defense establishment, industrialization, and socialization stand out as the dominant objectives of the Peiping regime in the particular pattern of resource allocation that is evident in Chinese Communist budgets. The timetable fixed for the achievement of these objectives has clearly given priority to the defense program, although since 1950, industrialization has received an increasing proportion of total budget allocations.

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The share of the allocation going to economic construction (industrialization) would be even greater if the allocation for social, cultural, and educational programs were grouped with it -- a grouping which appears legitimate because of the indoctrinational, state-oriented character of the so-called welfare programs. The allocation of resources through the budget is discussed in the following sections in terms of the five major categories of expenditure: economic construction; defense; social, cultural and educational; administration; credit, loans, and insurance and other. The categories are taken up according to their relative order of magnitude in the 1954 budget, and under each class a description is presented of the principal subcategories of expenditure falling thereunder with an estimate of these items based on 1954 budget data.

A. Economic Construction.

Expenditures for economic construction have continually favored heavy industry, a trend that is even more evident in the 1955 planned budget, which allocates roughly 6 billion yuan to heavy industry from economic construction funds of 14.2 billion yuan and a total budget of 29.7 billion yuan.

Information on the sector allocation of economic construction expenditures was first given in detail in the 1953 budget report, in which such expenditures were divided into the following five subclasses: industry; agriculture, forestry, and water conservancy; commerce, food, and foreign trade; transport and communications; and stockpiling, municipal construction, and investment in joint enterprises. In 1953, half of the economic construction funds were allocated to industry, which has received approximately that proportion ever since. In 1954, additional information was given to the effect that the industrial category was divided into 2 subclasses, with heavy industry receiving 78 percent of industrial funds and light industry the remainder. In 1955, this division was even more favorable to heavy industry, with the planned assignment to it of 89 percent of such funds.

Although the official budget reports have indicated substantial investment in railroads since 1950, no absolute figures were given until the 1955 planned budget. This shows railroad expenditures as two-thirds of all investment in transport and communications for the 1955 fiscal year, or 10 percent of total economic

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construction expenditures. The relative importance of railroad investment is made clear by the Five Year Plan, which calls for 5.67 billion yuan in railroad investment, a figure only 1 billion yuan lower than planned capital construction in the machine industries or in heavy industry.

In view of the predominantly agricultural nature of the Chinese economy, perhaps the most surprising aspect of the sector allocations is the small share for agriculture. Agriculture, forestry, and water conservancy received only 11 percent of 1954 economic construction expenditures, although this sector contributed the greatest proportion of national income. Furthermore, the Five Year Plan calls for agricultural production to increase at a yearly rate of over 3.5 percent, with no increase in state investment funds. Official discussions of the level of agricultural investment stress the importance of private investment in this sector. In fact the Five Year Plan estimate of private expenditure is about 2 billion yuan per year or 500 million yuan greater than state investment.

A significant shift in the proportionate allocation of economic construction funds is planned for 1955, when the requirements of the grain purchase and storage program raise the economic construction expenditures on commerce to 20 percent of the total, as compared with 14 percent in 1954. Expenditures on commerce, food, and foreign trade reflect the government's monopolization of trade in major agricultural commodities. Appropriations of this type have risen from roughly 1 billion yuan in 1953 to 2.8 billion yuan in 1955. The working capital requirements for execution of the agricultural procurement (forced-sales) program and, in general, for the socialization of trade are only partially represented by these appropriations, for the Chinese Communists have ruled that state and cooperative commercial enterprises must obtain most of their working capital from the state bank in the form of loans.

With reference to the allocations for "stockpiling, municipal construction and joint state-private enterprises," it is notable that this class of expenditures was not specified until the 1954 final budget report, although an unaccounted-for residual in the final budget of 1953 was assumed to represent this class. There is no information on the breakdown within the class, but the production level supports the conclusion that stockpiling has not been very important thus far. In respect to the subcategory of municipal

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construction, there is a possibility that this allocation may include primary and secondary schools, for the Budget Accounting Manual makes no other provision for such expenditures under the social, cultural, and educational category. On the other hand, there is a possibility that much of the required lower school construction may be financed by local extrabudgetary receipts, that is, outside the consolidated national budget.

As for the subcategory of joint enterprises, the regime's determined pressure toward socialization of industry and trade and the relevant investment requirements probably are the principal reasons for this subclass increasing from 800 million yuan in 1953 to the 1955 level of 1.5 billion yuan as the number of joint enterprises has risen rapidly during that period.

The allocation of expenditures for the category economic construction is presented in Table 11.

Table 11

Communist China: Allocation of Budgeted Economic Construction Expenditures, by Sector
1953-55

Sector	Percent		
	1953	1954	1955 Plan
Industry	49.8	46.4	45
Heavy	39	36.2	40
Light	10.8	10.2	5
Transport and communications	14.4	14.2	15.1
Agriculture, forestry, and water conservancy	13.2	11.1	9.3
Commerce, food, and foreign trade	11.6	14.3	20
Stockpiling, municipal construction, and joint enterprises	11	14	10.6
Total	<u>100</u>	<u>100</u>	<u>100</u>
Economic construction expenditures as a proportion of total expenditures	40.2	50.2	47.7

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On a functional basis, basic or capital construction expenditures* constitute the bulk of the economic construction category. The expenditure for fixed assets absorbed 63.5 percent of economic construction funds in 1954.

Working capital increments of state enterprises and co-operatives are the second largest subcategory under the category economic construction. Industrial enterprises are the principal recipients, receiving roughly 93 percent of the working capital appropriated through the budget.

Expenditures on repairs, operating expenses of budget-supported enterprises, and other items make up the balance of economic construction expenditures. The estimated breakdown of economic construction expenditures in 1954 is shown in Table 12.**

B. Defense.

Except for total expenditures, very little is known about defense spending, as this section of the budget is drawn up separately by the defense department, which has its own financial administration, independent of the Ministry of Finance. Only rough estimates of the general categories of expenditures can be made. Estimated wage payments and food and maintenance expenses of the 2.5 million troops constituted 15 percent of 1954 defense funds.*** The balance of 4.9 billion yuan covers weapons, supplies, and equipment (including imports), transport, training, and miscellaneous expenses.

* The basic construction figure given in budget reports cuts across the budget categories of economic construction; social, cultural, and educational programs; and administration. The breakdown of the 1954 figure was given by the State Statistical Bureau. It encompasses expenditures which increase fixed assets in any of these fields.

** Table 12 follows on p. 35.

*** Total wage payments per year equal 842 million yuan. 29/
Army cash wages are estimated at 150 yuan per year, plus maintenance expenses of 150 yuan per year per man. 30/ Navy and air personnel are estimated to get cash wages of 270 yuan per year per man and maintenance expenses of 190 yuan per year per man.

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Table 12

Communist China: Estimated Breakdown of Economic Construction
Expenditures, by Type of Expenditure
1954

Type of Expenditure	Proportion (Percent)	Amount (Million Yuan)
Basic construction	62.8	7,331.0 a/
Working capital	16.6	2,051.4 b/
Large-scale repair expenses	5.8	716.8 c/
Prospecting, equipment stockpiling, cash reserves, military land reclamation	8.5	1,050.4 c/
Residual		
Operating expenses, enterprise schools, experimental manufacture, cadre train- ing, and other residual expenditures	6.3	1,208.6
Total	100.0	12,358.2

a. Given in official breakdown of capital construction expenditures with an adjustment to include half of the unallocated funds. 31/

b. This represents a 50-percent increase in the Five Year Plan proportion of 11.1 percent for working capital. The upward adjustment is made on the assumption that the state made extra appropriations of working capital to correct the shortage which occurred in 1953.

c. Analogy to Five Year Plan.

Alternative views concerning the Chinese Communist allocation of resources to defense are either that they are understated by inclusion of defense spending in other budget categories or that the whole budget is understated to hide from the public the true level of defense spending.

The most important area of hidden defense spending is alleged to be in the category economic construction. There is believed to be some validity in the argument because military requirements to some extent influence the size of planned investment

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in heavy industry, and the capital construction and working capital requirements of the machine, aviation, shipbuilding, and communications equipment industries certainly provide in part for defense items. This argument is weakened, however, when any expenditure is called military which increases defense potential, such as heavy industry investment, for the budgets of other countries do not categorize such investment as part of defense spending.

As the total planned budget expenditures under the category economic construction for the six listed headings did not add up to the announced total allocation for the category economic construction in previous years, it has been assumed that the unspecified allocations were for secret military projects under the Second Ministry of the Machine Industry. The Budget Accounting Manual, however, specifically states that national defense construction is under the defense budget, and in China the munitions industry traditionally has been under the defense category. Furthermore, no mention is made of weapons and armaments industries being among those receiving economic construction funds. Thus it would appear that they are in fact included under the defense category.

There are items in all the other categories of the budget which are related to defense and might be labeled as hidden defense spending. These include pensions, disability aid, burial expenses, medical costs, and other compensation to soldiers and their families under the social, cultural, and educational category. Certain transport expenses of troops, at least during the Korean War, were listed under the category other. Wages, food, and maintenance for public security troops and expenses for the construction of border and coastal defenses cover a type of military activity which is listed under the administrative category.

A final element in the possible understatement of defense spending is for items that are financed outside the budget. Examples of this are the instances in which army units grow their own food crops and troops in transit are supplied locally with food, housing, and transport.

The second conclusion as to concealed defense spending was generated by announcements that a budget surplus was achieved in 1951. The ability of the Chinese Communist economy to support the war effort in Korea and still show a budget surplus was

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questioned. One surmise that was offered to explain such a surplus was that currency issue was used to cover some defense spending without recording either the receipts or the expenditures through the budget. A review of cumulative budget and price information suggests, as a more likely explanation, that secret Soviet military aid has been more extensive than was then believed likely.

The level of defense spending, even in the absence of any understatement, represents an imposing drain on Communist China's resources, amounting in 1954 to 24 percent of the total budget and 7 percent of GNP. Defense spending absorbed as much as 40 percent of budget funds in 1950 and 1951 and in 1955 was to receive 24 percent. Even at this lower share, defense spending is still the chief competitor of economic construction for available resources. The proportional shares of the two categories have moved almost exactly in reverse correlation, economic construction expenditures moving from 25 percent of the total in 1950 to 48 percent in the planned 1955 budget. The competitive relationship of these two categories is of special significance in analyzing the availability of funds for the Five Year Plan. For example, of the total increase in expenditures of 5 billion yuan planned in 1955 over 1954, economic construction received 1.9 billion, and defense received 1.4 billion yuan. It would appear that any substantial increase in defense spending over the 1955 level would be at the expense of the industrialization program.

C. Social, Cultural, and Educational.

Although compared with previous programs in these fields, the Chinese Communists have made great strides in building the physical facilities for schools, hospitals, and other welfare institutions, the social, cultural, and educational expenditures have never exceeded 16 percent of the budget, and the benefits to the individual have accrued as byproducts of a program geared primarily to meet the state's interest. The suballocations under the budget appropriation for social, cultural, and educational expenditures demonstrate that educational policy is geared solely to improving the quality of the labor force. The much vaunted relief funds are primarily loans to maintain agricultural production and to promote cooperativization. The principal cultural expenditures -- on press and broadcasting -- serve only to promote general acceptance of the Communist Party line. Educational expenditures are made in those areas vital to the national

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construction program or to meet political objectives such as propaganda to overseas Chinese. Relief and loan funds are available to those willing to join cooperatives or to other Party faithfuls rather than on the basis of need.

Certain items included in the social, cultural, and educational category pad the level of welfare expenditures when comparison is made to budgets of private enterprise economies. Investment in drug production, movies, publications, news agencies, and broadcasting are listed under this category as well as school and hospital construction. Subsidies to provide education for family members of Party cadres and to so-called people's organizations to provide popular support for the regime's programs are also considered social and educational expenses. Certain aspects of large-scale migration expenses, which are classed as social, might also be considered unique in that they cover expenses involved in forcing urban residents to move to rural areas.

Other expenditures under this general category are teachers' salaries; veterans' rehabilitation; anti-epidemic and antinarcotic campaigns; drama, art, and cultural activities; unemployment assistance; and rural relief.

The estimated disposition of funds under the category social, cultural, and educational in 1954 is shown in Table 13.*

D. Administration.

The expenditures under the category administration encompass both the normal political, judicial, and foreign relations expenses and the nontypical administrative expenditures on the vast labor reform (forced labor) program of Communist China and on the paramilitary public security forces.

The Chinese Communist vigorous attempts to keep scarce resources from being used for "nonproductive" administrative expenditures have met with some success. The absolute amount of administrative expenditures has increased by less than any other category of the budget, the relative share declining from 19 percent in 1950 to 7.5 percent in 1955. Some of the economy has been

* Table 13 follows on p. 39.

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Table 13

Communist China: Estimated Breakdown of Expenditures
under the Budget Category Social, Cultural, and Educational
1954

Million Yuan	
Type	Amount
Personnel	1,100 a/
Basic construction	895 b/
Relief	419.58 c/
Student allowances	154 d/
Veterans' pensions	198.02 e/
Residual	
Office expenses; travel; school, medical, and scientific equipment; library books, public security troops' clothing, sub- sidies, and other residual expenditures	694.01
Total	3,460.61

a. Estimate based on 2.5 million workers at an average annual wage of 400 yuan plus 10 percent for fringe benefits.

b. Given in official breakdown of 1954 basic construction expenditures. 32/

c. 33/

d. Estimate based on average monthly allowance of 10 yuan for living expenses plus 3 yuan for books, with approximately 1.1 million students receiving living expenses and 2.3 million receiving book allowances for 9 months of the year.

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rather artificial, with civil servants taking enforced wage cuts or losing such fringe benefits as free housing and medical care.

Despite the holding down of administrative expenditures, the Chinese Communists are using a relatively greater proportion of revenue for this type of activity than they consider desirable.

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Administrative expenditures are the only category of expenditure in which the Chinese Communists spend at a level proportionately close to that of the US.

The estimated breakdown of expenditures under the category administration for 1954 is presented in Table 14.

Table 14

Communist China: Estimated Breakdown of Expenditures
under the Budget Category Administration
1954

Million Yuan	
Type	Amount
Administrative, political, and legal units	
Personnel	630 a/
Other (residual)	602.07
Public security forces	390 b/
Basic construction	460 c/
Labor reform	80 d/
Total	<u>2,162.07</u>

a. Estimated 1.4 million employees (excluding labor reform guards and public security troops) at an average wage of 450 yuan per year.

b. Estimated 1.5 million troops at an average wage of 150 yuan and average expenses and equipment of 150 yuan each.

c. The breakdown of basic construction funds leaves 10.5 percent unallocated. Half of this portion is assumed to be for basic construction under the administrative category. 35/

d. Estimated 200,000 guards at an average wage of 300 yuan per year plus miscellaneous expenses. Other labor reform expenditures are included under basic construction and the residual components of this category. The food grown and used by labor camps is not recorded in the budget.

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E. Credit, Loans, Insurance, and Other.

The category credit, loans, insurance, and other includes repayment of principal and interest on foreign and domestic loans and extension of loans to other countries. These items are estimated to be about 516 million yuan of the 1954 expenditures of 838 million yuan, including about 296 million yuan in aid to North Korea and possibly 70 million yuan to North Vietnam. The insurance part of this account may be to provide for payment of unfunded insurance claims on the state insurance companies and possibly for allocations of statutory reserves for future indemnities. The remaining portion of this category includes certain tax collection expenses (including storage) and possibly some subsidies to political organizations, although the Budget Accounting Manual (see Appendix A) lists these under the social, cultural, and educational category.

These expenditures have never required a very large portion of the budget, a high of 7.8 percent being reached in 1953 and the average for the 5 years being about 5 percent. Payments into the general reserve fund were separated from these expenditures for the first time in 1955. Failure to meet reserve plans was probably the reason for the sharp drop in this type of spending in 1954 as compared with 1953. Overfulfillment of economic construction and defense spending in 1954 appears to have prevented a buildup of reserves.

The estimated breakdown of expenditures under the category credit, loans, insurance, and other in 1954 is shown in Table 15.*

IV. Five Year Plan and the Budget.

The problem of the adequacy of budgetary resources for investment requirements under the Five Year Plan lends itself to analysis by two different approaches. The first has to do with agriculture as the principal originating source of budgetary revenues, particularly with the possible effect on the budget of food-crop production falling short of the planned increase of 17.5 percent. The other approach relates to the estimated required 1957 budget expenditures as a proportion of the projected GNP. Both analyses tend to the conclusion that financing will not pose insurmountable difficulties in the accomplishment of the remaining portion of the Five Year Plan.

* Table 15 follows on p. 42.

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Table 15

Communist China: Estimated Breakdown of Expenditures
under the Budget Category Credit, Loans, and Insurance and Other
1954

Million Yuan	
Item	Amount
Repayment of principal and interest on 1950 Soviet loan	78 <u>a/</u>
Aid to North Korea	296 <u>b/</u>
Aid to North Vietnam	70 <u>c/</u>
Repayment of principal and interest on domestic bonds	72 <u>d/</u>
Short-term credit on international accounts, items in transit, insurance indemnities, and so on	322
Total	<u>838</u>

- a. Payment of first installment on loan of US \$300 million plus
1 percent interest on balance.
- b. 36/
- c. Estimated from articles delivered.
- d. 37/

A. Effect of Production Underfulfillment on the Budget.

The past and projected relationship of the budgetary system to economic development in Communist China points to the maintenance and increase of the level of budgetary receipts as one of the key factors in achieving the investment goals of the Five Year Plan. For the realization of the required level of income, Communist China must rely principally on profits and taxes from current production to support its planned investment program, for other sources of revenue have, from 1950 to 1955, diminished in relative proportions, and the principal alternative sources of revenue, internal capital levies and foreign loans, have never provided more than 11 percent of current receipts -- in fact, less than 10 percent in 1954.

It is apparent then that failure to meet production goals could cause underfulfillment of budget receipt plans and hence interfere with investment goals.

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Analysis of Communist China's present and planned production has led to the conclusion that agricultural production is the only area of probable production underfulfillment. Within agriculture the probable shortfall is confined to food crops because the relatively small amount of acreage devoted to commercial crops could be increased according to plan without undue strain on scarce resources. Food-crop production on the other hand constitutes the largest source of income in Communist China, and its maintenance requires the largest allocations of labor, land, and capital of any type of economic activity in the country. Without entering into an extensive analysis of the subject, reports of competent agricultural specialists are cited, which indicate that in order to achieve the very substantial increase of 17.5 percent predicated in the Five Year Plan, much more investment than is planned would be required. ^{38/} It is estimated that food-crop production will increase actually at about half the planned rate, or 9 percent over 1952.

The effect on budgetary receipts of this estimated shortfall of 50 percent may be gauged by determining what portions of present budget receipts are dependent on food-crop production. Dependence on food crops is defined to include such things as indirect taxes, profits on grain trade, food processing, and wine production. A breakdown of 1954 budget receipts indicates that 25 percent of receipts are dependent on supplies of food crops. If the Chinese Communists are planning on increased receipts on a scale proportionate to planned production increases, the planned receipts from food crops in 1957 would be 17.5 percent higher than in 1954. If the actual receipts, however, are only 9 percent higher, then the difference between planned and actual receipts from food-crop production would be roughly 600 million yuan. This sum represents about 1.7 percent of estimated 1957 expenditures and equals the excess of the estimated available receipts over the estimated expenditures in that year. It may be concluded, therefore, that underfulfillment of food-crop goals by the amount estimated does not represent a barrier to financing the Five Year Plan investment program.

The relationship of the various sources of revenue to total budget requirements is illustrated by the breakdown of 1954 receipts into the following three principal components: receipts dependent on food crops, receipts dependent on industrial crops, and receipts dependent on nonagricultural industrial production. Examples of the latter two classifications are profits and taxes on textile

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production, which are listed as industrial crop receipts, and profits and taxes on electric power, which arise in a nonagricultural industry.

The allocated receipts constitute 79 percent of current receipts in 1954. The unallocated receipts were roughly half in the form of credit, loans, insurance, and other, and half in the form of fees and taxes on services and property. The breakdown of budget receipts by sector of origin is shown in Table 16.*

As budget revenues from nonagricultural industry, revenues from the category other, and fees and taxes of services and property are dependent upon agricultural production only to the extent that economic activity in general requires the support of the agricultural sector, it is apparent that the increase of budget revenues in the nonagricultural sectors could not be hampered by any shortfall in achievement of agricultural goals other than a severe crop disaster for 2 or more years in succession. With a minimum increase in food crops of 9 percent over 1952 and with substantial achievement of the industrial crop goals the prospects for fulfillment of budgetary requirements to support the investment program under the Five Year Plan appear to be feasible.

B. Estimated Expenditures in 1957.

Government expenditure on goods, services, and investment in the last year of the Five Year Plan has been estimated at 34.3 billion yuan. The assumptions underlying the projection of both the total and of each category of expenditure yield expenditure figures consistent with the Chinese Communist plan to make 48 percent of capital investment in the last 2 years of the plan. These assumptions are given in the footnotes to Table 17,** which shows the estimated expenditures in the budget of 1957.

When the estimated expenditures are compared with estimated GNP by end use in 1957, they appear feasible. Output of investment goods based on physical production indexes plus government services will have a value of 35.1 billion yuan in 1957. In addition, as a portion of GNP, the estimated expenditures are only a slightly higher proportion of GNP than in 1954. This rise from 31 percent to 33 percent of GNP is certainly to be expected in view of increased socialization.

* Table 16 follows on p. 45.

** Table 17 follows on p. 46.

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The conclusion that the estimated expenditures are feasible depends on defense spending remaining at about the 1955 level of 7 billion yuan. It is believed that defense spending at a rate much in excess of this figure, at least within the Five Year Plan period, would interfere with economic construction goals.

Table 16

Communist China: Budget Receipts, by Sector of Origin
1954

Sector	Amount (Million Yuan)				Total	Proportion of Current Receipts (Percent)
	Profits of State Enter- prises ^a	Income Tax ^{b/}	Indirect Taxes ^{c/}	Agri- cultural Taxes ^{d/}		
Food crops	2,048	720	1,361	2,458	6,587	25
Industrial crops	2,040	447.5	2,703	819	6,009.5	23
Nonagricultural industry	5,873	471	1,875	0	8,219	31
Unallocated re- ceipts					5,420.5 ^{e/}	21
Total	<u>9,961</u>	<u>1,639</u>	<u>5,939</u>	<u>3,277</u>	<u>26,236</u>	<u>100</u>

a. Profits were estimated from value-added indexes based on physical production (1952 = 100), adjusted for an 8-percent price rise in 1954 over 1952. The state's share (includes one-half of joint enterprises) of industry (65 percent) and trade (50 percent) was taken from official announcements. The state shares of construction and of transport and telecommunications were estimated at 90 percent and 80 percent, respectively.

b. Income taxes were estimated by taking 20 percent of private income from industry, trade, transport, and construction and roughly 12 percent of private income from individual handicrafts and native transport. All figures are adjusted for an 8-percent rise.

c. Indirect taxes were estimated by applying official tax rates against gross value of production at producer prices. The totals were adjusted for an 8-percent price rise.

d. The total value of agricultural taxes given in the budget was allocated in accordance with the proportion of gross value of industrial and food crops.

e. This is made up of the following budget data: credit, loans, and insurance, 2,345 million yuan; other receipts, 712 million yuan; miscellaneous taxes and fees, 969 million yuan; and taxes and fees on services, 1,394.5 million yuan. The latter figure is a residual.

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Table 17

Communist China: Estimated Expenditures in the Budget
1957

Category	Expenditure	
	Million Yuan	Percent of Total
Economic construction	19,770 <u>a/</u>	57.6
Social, cultural, and educational	2,550 <u>b/</u>	7.4
Defense	7,200 <u>c/</u>	21.0
Administration	2,400 <u>d/</u>	7.0
Other	2,400 <u>e/</u>	7.0
Total	<u>34,320</u>	<u>100.0</u>
Basic construction	13,333 <u>f/</u>	38.9

a. The expenditures for 1953 through 1955 (assuming the latter were 100 percent fulfilled) were subtracted from the Five Year Plan goal of 62.4-billion-yuan expenditure on economic construction. The balance was adjusted for an estimated 25-percent rise in investment prices by the end of 1954. Prices are assumed to remain constant after 1954. Half the balance is assumed to be spent in 1957.

b. The 1953 through 1955 expenditures (assuming the latter were 95 percent fulfilled) were subtracted from the Five Year Plan goal of 14.27-billion-yuan expenditure on social, cultural, and educational departments. The balance was adjusted for an estimated 10-percent rise in prices by the end of 1954.

c. Defense spending is assumed to level off at the 1955 level. Expenditures for nonrecurring transfer of Soviet assets, such as those at Port Arthur in 1955, are assumed to be replaced in 1957 by increases in other areas of defense spending.

d. Assumes a 150-million-yuan rise over 1955 to cover increased control apparatus of the government.

e. Assumes continuation of 1955 allocations to reserves and other purposes, with a slight increase to cover repayment of Soviet loans and the 1954 and 1955 domestic bonds.

f. Half of the remaining basic construction expenditures are adjusted for 25-percent price rise by the end of 1954, assuming 1955 planned expenditure was 100 percent fulfilled.

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APPENDIX A

CLASSIFICATION OF THE REVENUE AND EXPENDITURE ACCOUNTS

The titles of the major and component revenue and expenditure accounts listed in this glossary are extracted from the Chinese Communist official Budget Accounting Manual. The manual is helpful in analyzing the accounts, although in some instances it is not clear to which major account a subcategory belongs. For example, category S -- business revenues of government -- could either be under profits of state enterprises or under the category other receipts. The latter interpretation is used in this report, although the manual does not state the actual practice.

I. Revenues.

A. Agricultural Taxes.

1. Summer levy: grain, commercial crops, commutation to cash
2. Autumn levy: grain, commercial crops, commutation to cash
3. Payment in arrears of previous years: grain, commercial crops, commutation to cash
4. Pastoral taxes

B. Commodity Tax Revenues.

1. Tobacco and spirits taxes
2. Firecrackers and religious articles
3. Cosmetics
4. Taxes on food and beverage
5. Taxes on fiber, skin, and leather
6. Taxes on sundry goods
7. Taxes on manufactured goods
8. Taxes on mineral and wood products

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C. Industrial and Commercial Tax Revenues.

1. Taxes on state-operated enterprises
2. Taxes on subordinate government enterprises
3. Taxes on cooperative enterprises
4. Taxes on joint public-private enterprises
5. Taxes on private industrial and commercial enterprises
6. Special assessment on business
7. Temporary commercial business taxes
8. Taxes on peddlers

D. Industrial and Commercial Income Tax Revenues.

1. Income taxes on government enterprises
(other than national)
2. Income taxes on cooperative enterprises
3. Income taxes on public-private enterprises
4. Income taxes on private enterprises
5. Other income taxes

E. Stamp Tax Revenues.

F. Revenues from Taxes on Income from Interest.

G. Customs Revenues.

1. Import duties
2. Export duties
3. Tonnage dues

H. Salt Tax Revenues.

1. Taxes on table salt
2. Salt export tax
3. Tax on fish salt
4. Tax on industrial salt
5. Tax on agricultural salt
6. Tax on salt byproducts

I. Consolidated Sales Tax.

1. Taxes on cloth and thread
2. Other consolidated sales taxes

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J. Local Taxes.

1. Slaughtering
2. Transactions taxes
3. Deeds
4. Real estate (buildings and land)
5. Special consumption taxes (luxury banquet)
6. License taxes (vehicles)
7. Special production taxes (applicable only to Manchuria)
8. Local surtaxes (must be approved by next higher level government and must not be increased greatly)
 - a. Agricultural surtaxes
 - b. Industrial and commercial surtaxes
 - c. Real estate surtaxes
 - d. Surtaxes on public utilities
 - e. Other surtaxes

K. Income from Land Deeds (issued after land reform).

L. Income from Monopolies (shared by central and local governments).

1. Tobacco monopoly
2. Spirits monopoly
3. Other monopolies

M. Revenues from Profits of Government Enterprises.

1. Profits of heavy industry
2. Profits of fuel industries
3. Profits of textile mills
4. Profits of light industry
5. Profits of railroads
6. Profits of posts and telegraphs
7. Profits of communications
8. Profits of agriculture (including pastoral enterprises and fishing)
9. Profits of forestry
10. Profits of water conservancy
11. Profits of banking
12. Profits of trading

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13. Profits of insurance
14. Profits of salt production
15. Profits of monopoly construction enterprise
16. Profits of drugs manufacturing
17. Profits of cultural institutions (including firms
for manufacturing scientific instruments)
18. Profits of public utilities
 - a. Water companies
 - b. Urban communication companies
 - c. Gas and electric companies
 - d. Public construction companies
 - e. Other companies
19. Profits of joint public-private enterprises
20. Profits of other enterprises

N. Revenue from Payments by Government Enterprises
into the General Depreciation Fund.

1. Heavy industry
2. Fuel industries
3. Textile mills
4. Light industry
5. Railroads
6. Posts and telegraphs
7. Communications enterprises
8. Agriculture
9. Forestry
10. Water conservancy
11. Banking
12. Trading
13. Insurance
14. Salt production
15. Monopoly enterprises
16. Pharmacological enterprises
17. Cultural enterprises
18. Public utilities
 - a. Water companies
 - b. Urban communication companies
 - c. Gas and electric companies
 - d. Public construction companies
 - e. Other companies
19. Other enterprises

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- O. Revenue from Business Operations and Rental Receipts of Government Enterprises.
 - 1. Business operations
 - 2. Rental operations
- P. Revenue from the Sale of Fixed Assets of Government Enterprises.
- Q. Revenue from Reimbursements made by Government Enterprises from Their Working Capital (includes repayments from working capital of cooperatives).
- R. Revenue from Increase in Appraised Value of Goods.
 - 1. Heavy industry
 - 2. Fuel industries
 - 3. Textile mills
 - 4. Light industry
 - 5. Railroads
 - 6. Posts and telegraphs
 - 7. Communications enterprises
 - 8. Agriculture
 - 9. Forestry
 - 10. Water conservancy
 - 11. Banking
 - 12. Trading
 - 13. Insurance
 - 14. Salt production
 - 15. Monopoly enterprises
 - 16. Pharmacological enterprises
 - 17. Cultural enterprises
 - 18. Public utilities
 - a. Water companies
 - b. Urban communication companies
 - c. Gas and electric companies
 - d. Public construction companies
 - e. Other companies
 - 19. Other enterprises

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S. Business Revenues of Government.

1. Economic construction (agriculture, water conservancy, and other revenues from economic construction)
2. Educational
3. Cultural
4. Social
5. Medical
6. Public utilities
7. Assessment on land and property
8. Other business revenues

T. Administrative Revenues.

1. Fines (administrative, court, police, taxation fines, salt tax fines to central government, other to province and municipality, other fines)
2. Fees (administrative, court, police, medical -- including slaughtering and inspection)

U. Revenues from Public Property.

1. Income from rental
2. Income from increase in value of public property
3. Income from interest on public funds
4. Income from warehouse clearance (cash from sale and increase in value, probably Chinese Nationalist government property)
5. Income from disposal of enemy property

V. Revenue from Public Loans.

1. Domestic
2. Foreign
3. Income from repayment of funds loaned abroad

W. Other Revenues.

1. Revenue from production by military units
2. Revenue from contributions
3. Revenue from production by labor reform
4. Miscellaneous

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- X. Revenue Forwarded by Lower Level to Higher Level Governments.
- Y. Revenue from Subsidies by Higher Level to Lower Level Governments.
- Z. Revenue from Previous Year's Surplus.
- AA. Revenue from Currency Issue (applies to central government only).

II. Expenditures.

A. Defense.

- 1. National defense expenditures (National Revolutionary Military Committee and defense construction)
- 2. Military affairs expenditures (mobilization of local military forces)

B. Economic Construction.

- 3. Heavy industry
- 4. Fuel industries
- 5. Textile industries
- 6. Light industry
- 7. Railroads
- 8. Posts and telegraphs
- 9. Communications and transport
- 10. Agriculture and conservancy
- 11. Forestry
- 12. Water conservancy (large-scale irrigation, flood control, hydroelectricity)
- 13. Banking expenditures (costs of operations)
- 14. Insurance expenditures
- 15. Trade and commerce (domestic and foreign)
- 16. Salt production
- 17. Monopolies (tobacco and spirits)
- 18. Investment in joint public-private industries (shares)
- 19. Costs of other investment in corporation, including grain processing
- 20. Municipal construction (housing and public utilities)
- 21. Surveying of natural resources

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- 22. Construction of storage facilities
- 23. Cooperatives

C. Social and Cultural Expenditures.

- 24. Cultural (film, drama, music, fine arts)
- 25. Educational (adult training, normal schools, and universities)
- 26. Training of cadres
- 27. Scientific (research, experimentation)
- 28. News (newspapers, photography, broadcasting)
- 29. Publishing (copyright, translation, printing, publications)
- 30. Public health
- 31. Social (support for disabled workers, relief to families of soldiers)

D. Subsidies to Political Parties and Mass Organizations.

- 32. Subsidies to political parties and mass organizations

E. Administrative.

- 33. Administrative organization control expenditures (central, regional, provincial, municipal, hsien)
- 34. Political affairs (popular assemblies, nationalities affairs, overseas affairs, land reform, political propaganda, celebration of national holidays)
- 35. Foreign relations
- 36. Public security and judicial expenditures

F. Fiscal (cost of collections of taxes).

- 37. Fiscal expenditures -- customs, salt, general

G. Other Expenditures.

- 38. Expenditures on public loans both foreign and domestic, payment of interest and principal
- 39. Subsidies to local governments
- 40. Funds remitted to higher level governments by lower level governments
- 41. Expenditures on storage of valuables
- 42. Other
- 43. General reserves

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APPENDIX B

METHODOLOGY

I. Reclassification of Gross National Product.

The GNP sector-of-origin accounts for 1954 have been regrouped into four accounts in Table 4*: these are agriculture, forestry, and fishing; private nonagriculture; state enterprises; and indirect taxes. The purpose of the regrouping is to show the relationship of a particular sector's actual and imputed income to budget receipts drawn from that sector.

The components of the income from agriculture, forestry, and fishing are first the value of such production (including home industry but net of production expenses) based on a physical production index (1952 = 100) adjusted for an 8-percent rise in grain prices in 1954 over 1952. 39/ Some of the wage payments by state enterprises go to peasants and are not reflected in the valuation of home industry. The income based on production indexes does not include rent, and so rent has been imputed at the rate of 5.2 percent of net farm income.

Wage payments to government employees have been divided between the private agriculture and nonagricultural sectors. This division, on the basis of which group uses the services rendered is an alternative to listing these wage payments separately with their tax payments. The former method is used on the grounds that the government services augment peasant income and should be taken into consideration in relating tax collections to sector income.

Private nonagricultural income was taken from indexes of physical production valued at factory prices. For certain sectors it was possible to use official announcements of the proportion of output contributed by private enterprise. The announced private ownership in 1954 was 35 percent of modern industry and 50 percent of trade. All of individual handicraft and native transport was treated as private value added. The private

* P. 15, above.

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ownership of the remaining two sectors was estimated to be 20 percent of modern transport and communications and 10 percent of construction. This gave a total value added in private industry and trade of 16.26 billion yuan: modern industry, 3.81 billion yuan; trade, 4.48 billion yuan; modern transport and communications, 0.43 billion yuan; construction, 0.35 billion yuan; native transport, 3.91 billion yuan; and individual handicraft, 3.28 billion yuan.

The value of consumer services, which was based on the labor force, was added to this sector. One-third of the value of government services, that is, the wage payments to government employees, was added to this sector. In the division of the value of these services between agriculture and nonagriculture, double the proportion to total population was attributed to the nonagriculture sector. Wage payments totaled 4,816 million yuan, with the following breakdown: troop wages, 872 million yuan; supporting defense personnel, 872 million yuan; health, education, and welfare wages, 1,100 million yuan; transfer payments, 872 million yuan; administrative wages, 630 million yuan; public security troops, 390 million yuan; and labor reform wages, 80 million yuan.

Wage payments by state enterprises were the final addition to the income of this sector. These wage payments include bonuses and welfare expenditures from that portion of profits retainable for the purpose (that is, 5 percent of planned and 20 percent of excess profits -- a maximum of 15 percent of the wage bill). ^{40/} Basic wages for the estimated 6.4 million full-time state enterprise employees total 4.83 billion yuan. Fringe benefits, bonuses, and payments to casual labor raise the wage payments to about 6.6 billion yuan.

The value added by state enterprises is derived in the same way as private income from trade and industry. Wage payments to peasant and nonagricultural labor accounted for somewhat less than half, and the balance equaled the profits and depreciation reserves which are remitted in total to the national treasury.

Indirect taxes were listed separately because the prices at which the output of the other sectors was valued excluded such taxes.

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APPENDIX C

GAPS IN INTELLIGENCE

There are gaps in intelligence throughout the budget of Communist China. The budget reports give no details on the accounts making up the major categories, and scattered information from other sources is inadequate for almost all categories.

On an over-all basis, it is not clear whether there is financing outside the consolidated national budget and, if so, the extent of it. The particular areas in which extrabudgetary financing may be important are primary and secondary education and hsiang (town) level administrative expenses.

The amount and category listing of subsidies to political parties is another area of uncertainty on the expenditure side.

There are several types of receipts, the magnitude and manner of listing of which require more intelligence. The amount and character of Soviet loans is one type requiring clarification. Along the same line, the amount, if any, of credit by the European Satellites is unknown. Within the same major category of credit, loans, and insurance, it would be helpful to know the distinction between the insurance receipts and those listed under profits of state enterprises.

Two budgetary items which may be related are surplus funds and receipts from the "Five Anti" campaign. The source of the surplus cannot be determined from present budget reports. The "Five Anti" receipts are a puzzle as to amount and manner of listing.

Other revenue items about which additional information is required are the value at which agricultural taxes are listed, the amount of profits made on state grain trade, the sources of receipts of budget-supported enterprises, and the composition of miscellaneous taxes.

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APPENDIX D

SOURCE REFERENCES

Evaluations, following the classification entry and designated "Eval.," have the following significance:

<u>Source of Information</u>	<u>Information</u>
Doc. - Documentary	1 - Confirmed by other sources
A - Completely reliable	2 - Probably true
B - Usually reliable	3 - Possibly true
C - Fairly reliable	4 - Doubtful
D - Not usually reliable	5 - Probably false
E - Not reliable	6 - Cannot be judged
F - Cannot be judged	

"Documentary" refers to original documents of foreign governments and organizations; copies or translations of such documents by a staff officer; or information extracted from such documents by a staff officer, all of which may carry the field evaluation "Documentary."

Evaluations not otherwise designated are those appearing on the cited document; those designated "RR" are by the author of this report. No "RR" evaluation is given when the author agrees with the evaluation on the cited document.

All sources are evaluated RR 2 unless otherwise indicated.

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